

D.T.E. 00-75

Petition of Sheffield Water Company, pursuant to G.L. c. 164, § 14 and G.L. c. 165, § 2, to issue a long-term note in the principal amount of up to \$150,000, to finance the installation of water meters and related equipment.

APPEARANCE: Dana A. Bartholomew, President

Sheffield Water Company

1081 South Undermountain Road

Sheffield, Massachusetts 01257

Petitioner

I. INTRODUCTION

On September 28, 2000, Sheffield Water Company ("Sheffield" or "Company"), pursuant to G.L. c. 164, § 14 and G.L. c. 165, § 2, filed a petition with the Department of Telecommunications and Energy ("Department") requesting approval of a proposed long-term financing in the principal amount of up to \$150,000. The Company seeks to issue a twenty-year note in order to finance the installation of water meters and related equipment (Exh. SWC-1).

Pursuant to notice duly issued, an evidentiary hearing was held at the offices of the Department on November 29, 2000. No petitions for leave to intervene were filed. At the hearing, the Company presented two witnesses in support of its petition: Dana Bartholomew, president of the Company and Colin Smith of Smith, Watson and Company, LLP. The evidentiary record consists of nine exhibits and two responses to Department record requests.

II. STANDARD OF REVIEW

In order for the Department to approve the issuance of stocks, bonds, coupon notes, or other

types of long-term indebtedness⁽¹⁾ by a water company, the Department must determine that the proposed issuance meets two tests. First, the Department must assess whether the proposed issuance is reasonably necessary to accomplish some legitimate purpose in meeting a company's service obligations, pursuant to G.L. c. 164, § 14.⁽²⁾ Fitchburg Gas &

Electric Light Company v. Department of Public Utilities, 395 Mass. 836, 842 (1985) ("Fitchburg II"), citing Fitchburg Gas & Electric Light Company v. Department of Public Utilities, 394 Mass. 671, 678 (1985) ("Fitchburg I"). Second, the Department must

determine whether the Company has met the net plant test.⁽³⁾ Colonial Gas Company,

D.P.U. 84-96 (1984); see also Milford Water Company, D.P.U. 91-257, at 4-5 (1992); Edgartown Water Company, D.P.U. 90-274, at 5-7 (1990); Barnstable Water Company, D.P.U. 90-273, at 6-7 (1990).

The Supreme Judicial Court has found that, for the purposes of G. L. c. 164, § 14, "reasonably necessary" means "reasonably necessary for the accomplishment of some purpose having to do with the obligations of the company to the public and its ability to carry out those

obligations with the greatest possible efficiency." Fitchburg II at 836, citing Lowell Gas Light Co. v. Department of Public Utilities, 319 Mass. 46, 52 (1946). In cases where no issue exists about whether management decisions regarding the requested financing were the result of a reasonable decision-making process, the Department limits its § 14 review to the facial reasonableness of the purpose to which the proceeds of the proposed financing will be put. Canal Electric Company, et al., D.P.U. 84-152, at 20 (1984); see, e.g., Colonial Gas Company, D.P.U. 90-50, at 6 (1990).

The Fitchburg I and II and Lowell Gas cases also established that the burden of proving that an issuance is reasonably necessary rests with the company proposing the issuance, and that the Department's authority to review a proposed issuance "is not limited to a 'perfunctory review.'" Fitchburg I, at 678; Fitchburg II, at 842, citing Lowell Gas, at 52.

Regarding the net plant test, a company is required to present evidence showing that its net utility plant (original cost of capitalizable plant, less accumulated depreciation) equals or exceeds its total capitalization (the sum of its long-term debt and its preferred and common stock outstanding, exclusive of retained earnings) and will continue to do so following the proposed issuance. Colonial Gas Company, D.P.U. 84-96, at 5 (1984).

III. DESCRIPTION OF THE PROPOSED FINANCING

The Company requests approval by the Department to incur long-term indebtedness in the principal amount of \$150,000 from Canaan National Bank ("Canaan"). According to the Company, the proceeds of the loan will be used to finance the installation of water meters and related equipment (Exh. SWC-1; Tr. at 6). The Company represented that the installation of meters provides for a more equitable way to bill customers for actual water consumption (*id.*).⁽⁴⁾ The Company stated that the note will have a maturity date of no later than 20 years from the date of issuance, and carry a variable interest rate based on the published Wall Street Journal Prime rate ("Prime") plus an interest rate spread of zero percent, which is currently

9.5 percent (Exh. SWC-2; RR-DTE-1; Tr. at 5-6, 16-21, 30, 33). The Company explained that the interest rate can be reviewed every five years at Canaan's option (id.). The Company stated that while Canaan initially proposed an interest rate equal to Prime plus one percent, it later agreed to offer Sheffield a more favorable interest rate of Prime plus zero percent (id.).

Sheffield stated that it sought a bid for the proposed financing from Berkshire Bank ("Berkshire"), which offered an interest rate of 9.75 percent and a review period of three years, but considered Canaan's proposed interest rate of 9.5 percent and a review period of five years more favorable to the Company (RR-DTE-2; Tr. at 19-20). In addition, Sheffield asserted that because it has established a long-standing relationship with Canaan, choosing another lending institution might result in significant up-front costs⁽⁵⁾ that would not be incurred from Canaan (Tr. at 13-18).

III. CAPITAL STRUCTURE OF THE COMPANY

The Company's utility plant in service, as of December 31, 1999, is \$438,894, with accumulated depreciation of \$180,326 (Exh. DTE 1-3). Thus, as of December 31, 1999, the Company has a net utility plant, excluding accumulated depreciation, of \$258,568 (id.). As of December 31, 1999, the Company reported a total capitalization of \$77,724, consisting of long-term debt of \$57,724 and common stock of \$20,000 (id.).

IV. ANALYSIS AND FINDINGS

The Company intends to use the proceeds of the proposed long-term indebtedness with Canaan to install water meters and related equipment. The Company states that the installation of water meters provides for a more equitable way to bill customers for actual water consumption. While the Department makes no conclusions at this time on the prudence of the Company's capital expenditures, it is clear that water meters represent physical plant customarily used by water companies. Accordingly, the Department finds that Sheffield's proposed long-term indebtedness is reasonably necessary to accomplish the legitimate purpose of installing water meters and related equipment.⁽⁶⁾

In Blackstone Gas Company, D.T.E. 98-91, at 5 (1999), the Department directed "all companies, at a minimum, to indicate whether they sought alternative forms of financing or contacted other lenders to demonstrate that their proposed financing was cost effective." The Department recognizes the difficulties encountered by smaller companies in accessing capital markets. Generic Cost of Equity for Water Companies, D.P.U. 96-90-A at 8-9 (1997). The Company, in this instance, obtained loan terms from two banks, Canaan and Berkshire. The Company explained that it chose Canaan over Berkshire for the following three reasons:

(1) a lower interest rate charged by Canaan versus that offered by Berkshire; (2) the five-year review period offered by Canaan versus the three-year period proposed by Berkshire;

and (3) Sheffield's long-standing relationship with Canaan allows Sheffield to avoid up-front costs associated with beginning a new relationship with another lending institution

(RR-DTE-2; Tr. at 13-18). The Department finds that the Company has made a reasonable effort to seek multiple options for securing the proposed financing given the limited access to the

financial markets for a company such as Sheffield.

With respect to the net plant test, as of December 31, 1999, the Company's utility plant in service was \$438,894, with accumulated depreciation of \$180,326, resulting in net utility plant of \$258,568 (Exh. DTE 1-3). The net utility plant less the Company's total capitalization of \$77,724 yields an excess of net utility plant in service over outstanding capital of \$180,844 (id.). The proposed new financing of \$150,000 would increase the Company's total capitalization to \$227,724, resulting in an excess of net utility plant over outstanding capital

of \$30,844. Therefore, the Department finds that the Company's proposed financing meets the net plant test.

Issues concerning the prudence of the Company's financing have not been addressed in this proceeding, and the Department's decision in this case does not represent a determination that any project is economically beneficial to the Company or its customers. The Department emphasizes that its determination in this Order shall not in any way be construed as a ruling relative to the appropriate rate-making to be accorded any costs associated with the proposed financing.

V. ORDER

Accordingly, after due notice, hearing, and consideration, the Department hereby

VOTES: That the execution of a twenty-year note by Sheffield Water Company in the principal amount of \$150,000 payable to Canaan National Bank, at a variable interest rate equal to the published Wall Street Journal Prime rate with a five-year review period, is reasonably necessary for the purposes for which it is proposed; and it is

ORDERED: The Sheffield Water Company shall be authorized to enter into a twenty-five year loan agreement in the principal amount of \$150,000 payable to Canaan National Bank, at a variable interest rate equal to the published Wall Street Journal Prime rate with a five-year review period; and it is

FURTHER ORDERED: That the Secretary of the Department shall within three days of the issuance of this Order cause a certified copy of it to be filed with the Secretary of the Commonwealth.

By Order of the Department,

James Connelly, Chairman

W. Robert Keating, Commissioner

Paul B. Vasington, Commissioner

Eugene J. Sullivan, Jr., Commissioner

Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).

1. Long-term refers to periods of more than one year from the date of issuance.

G.L. c. 164, § 14.

2. The provisions of G.L. c. 164, § 14 are applied to water companies pursuant to

G.L. c. 165, § 2.

3. The net plant test is derived from G.L. c. 164, § 16.

4. The Company also filed a separate petition seeking a rate increase with the Department, docketed as D.T.E. 00-76.

5. The Company stated that up-front costs would include such costs as legal fees and appraisal fees (Tr. at 15).

6. The prudence of the Company's metering project is more appropriately considered in Sheffield's current rate case proceeding, D.T.E. 00-76.